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¶1. (U) Summary. This is Volume 8, Issue 5 of U.S. Embassy Pretoria's South Africa Economic News Weekly Newsletter.

Topics of this week's newsletter are:
- Foreign Sell-off Imperils Rand, Current Account
- Inflation Rises above Forecasts
- MPC Leaves Repo Rate Steady at 11%
- Banks Expected to Post Robust Profits
- Metrorail Unveils Expansion Plans
- MTN Outsources IT Services to IBM
- Hi-Tech Prawn Farming to Create Jobs
- Not So Fast - South Africa Still on Top for Gold Production
- Record High Gold and Platinum Prices
- Government Reassures Investors
- CEF Funds Solar-powered Traffic Lights
End Summary.

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Foreign Sell-off Imperils Rand, Current Account
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¶2. (U) Foreigners have sold up to R8 billion ($1.1 billion) of local bonds and equities since January 24, making January the third consecutive month of net sales for South Africa. Apart from hurting the rand and threatening the current account, which is financed through foreign inflows, it will cause the South African Reserve Bank (SARB) to use hard-won reserves to shore up the deficit. Those reserves were part of the reason that ratings agencies upgraded South Africa's international credit status. Global financial house CITI said the large net sales came after offshore accounts that were heavily invested in precious metals learned that some mines were shut down due to power shortfalls. According to CITI, the last time foreigners were dumping domestic stocks and bonds was in 2003, but back then the current account deficit was 1.1% of GDP compared to 8.1% in the third quarter of
¶2007. According to the latest statistics from the JSE and the Bond Exchange of South Africa, foreigners have sold off 171% more in equities than they had at this time last year. The bond market was also trending towards net sales for the month (?). While many analysts view the sell-off as a change in risk appetite, Rudolph Vermeulen, a derivatives trader at online brokerage Global Trader,

said some investors were just taking their profits in an attempt to weather stormy markets elsewhere in the world. (Business Day, January 30, 2008)

Inflation Rises above Forecasts

¶3. (U) According to Statistics South Africa data, CPIX inflation (consumer price inflation less mortgage interest rates) surged from 7.9% y/y in November 2007 to 8.6% y/y in December, racing further away from the 3 to 6% target band. Originally, a Reuters poll forecasted that CPIX would rise to 8.5% y/y in December. "The number is a little bit higher than the market expected. The market has been saying news on inflation is likely to get worse before it gets better," Nedbank senior economist Nicky Weimer said. A cumulative 400-basis point interest rate hike since June 2006 has failed to stem inflation, spurred largely by rising global food and fuel costs. Local petrol pump prices rose by 6.1% in its monthly adjustment in December. The rand weakened from R7.22 to R7.27 against the dollar after the data was released. (Business Day, January 30, 2008)
Q(Business Day, January 30, 2008)

MPC Leaves Repo Rate Steady at 11%

The Monetary Policy Committee (MPC) kept the repo rate steady at 11.0% on January 31, in line with expectations, despite a further surge in inflation last month. This leaves the prime interest rate at 14.5%. South African Reserve Bank Governor Tito Mboweni said there were still considerable risks to the inflation outlook, but economic growth was expected to slow, although there were no indications of a recession in Africa's biggest economy. "In the light inter-alia of heightened economic uncertainties, both domestically and globally, and some evidence of moderation in domestic expenditure, the MPC has decided that it is appropriate

at this time to leave the repo rate unchanged at 11%," he said in a televised statement. The decision follows four consecutive 50-basis-point increases since June 2007 and a cumulative 400-basis-point hike since June 2006 as the MPC battled to tame inflationary pressures. (Business Day, January 31, 2008)

Banks Expected to Post Robust Profits

¶5. (U) Standard & Poor's (S&P) said South African banks are expected to post robust profits and asset quality as a result of strong growth in business and the absence of exposure to sub-prime mortgages. But the rating agency said banks also faced growing macro-economic and political risks from rising inflation in an overheating economy and uncertainty over the presidential succession next year. "Balancing these opposing forces over the coming months will be the central challenge for the country's big four banks - Absa Bank, FirstRand Bank, Nedbank and Standard Bank - that collectively hold more than 80% of South Africa's banking assets," S&P said in its report entitled, "South African Banks Balance Robust Growth With Rising Risks in 2008." "GDP growth rates of 5 to 6% in South Africa over the past five years, as well as deregulation in the banking sector, have contributed to strong earnings growth for the banks," said S&P South Africa and Sub-Saharan Africa Managing Director. However, a local analyst indicated that the "domino effect" of the power crisis could dampen growth prospects. S&P said growth in the banking sector was "likely to slow somewhat" this year, as inflation was still well above the upper end of the Reserve Bank's target range and interest rates were high at 11%, and were expected to increase further in the first quarter of 2008. "With significant infrastructure projects coming on stream, partly in preparation for the 2010 World Cup, we still expect this year to be a positive year for bank revenues," S&P Credit Analyst Jerome Chui said.

(Business Day, January 29, 2008)

Metrorail Unveils Expansion Plans

¶6. (U) Metrorail CEO Lucky Montana has embarked on an R18 billion ($2.5 billion) strategy aimed at stabilizing the company by 2010. Improving train punctuality, reliability, customer service and commuter safety are at the top of his agenda. Montana took over at Metrorail in July 2006 after it was transferred from Transnet to the Department of Transport's South Africa Rail Commuter Corp. The strategy includes upgrading rail infrastructure; ensuring train frequencies during peak hours; extending daily operating hours; and addressing commuter confidence. He reported that ageing assets and insufficient rolling stock challenge Metrorail operations. About 2 million South Africans use trains daily and there has "been under investment in rail going back over 30 years," said Montana. The average age of the fleet is 40 years and only about 3,000 of its 4,600 coaches are operational. Montana says this lack of capacity is one of the main reasons for the company's shrinking service and inability to meet demand. He Qthe company's shrinking service and inability to meet demand. He aimed to have 96% of the fleet on the tracks by 2010. He added that Metrorail intends to expand its service in the next two years. Planned new lines will offer service to the FNB soccer stadium in Johannesburg, which will host the 2010 soccer World Cup final, as well as to Durban's King Senzangakhona and Soweto's Orlando stadiums. (Financial Mail, January 25, 2008)

MTN Outsources IT Services to IBM

¶7. (U) MTN South Africa has outsourced its information systems division, which looks after its technology services, to IBM. MTN Managing Director announced that in "a number of business areas, MTN partners with globally recognized best-of-breed service providers like IBM, to gain access to best practice and international core competencies for the benefit of its own business and to enable MTN to provide world-class services to its customers." The deal was rumored to be worth an estimated R1 billion ($138 million). MTN has annual revenues of R25 billion ($3.5 billion). IBM Country General Manager said the agreement

would enable MTN to tap into IBM's global experience in the implementation of innovative solutions similar to those of global telecoms operators. (Business Report, January 29, 2008)

Hi-Tech Prawn Farming to Create Jobs

¶8. (U) Sea Ark Afrika, a subsidiary of the Bosasa Group of Companies has established a pilot hi-tech prawn farm project at the Coega Industrial Zone in Port Elizabeth. Prawn farming is traditionally conducted in open-air ponds, which makes prawns susceptible to disease and results in farming losses. This new project, regarded as a first of its kind, will operate in a bio-secured and disease-free facility. High quality diets and filtered water will be provided. The project will involve the development of a 1,200 hectares farming facility following a successful pilot phase. The final project is expected to be completed in 2014 at a cost of R9.2 billion ($1.3 billion). A Sea Ark official noted that research and development for the project was conducted in both the U.S. and South Africa at a cost of $40 million. Sea Ark Afrika President David Wills described the facility as a "sustaining, job-creating and technologically innovating project". Wills said the farm is expected to create 11,800 jobs, with 1,000 jobs slots slated specifically for women. (Engineering News, January 18-25, 2008)

Not So Fast - South Africa Still on Top for
Gold Production

¶9. (U) Early estimates showed that China had overtaken South Africa as world leader, but more recent reports confirm that South Africa topped China's gold output in 2007, with 272 tons to 270.5 tons, respectively, according to the China Gold Association. The two countries were neck in neck in gold output in the second half of the year, leading London-based GFMS to estimate that China had already become the world's largest producer, and prompting hand-wringing in South Africa. South African output has been constrained by dwindling ore grades, accidents, rising labor costs, and - most recently - by power disruptions. New South African deep mines still show great economic mineral potential. (Pretoria News, January 30, 2008)

Record High Gold and Platinum Prices

¶10. (U) Gold and platinum hit all-time highs on January 25, after a power crisis closed South African mines. South Africa's three main gold producers and the world's largest platinum miner suspended production, sending precious metal prices to new highs. Spot gold hit an intraday high of $922.40 an ounce, surpassing last week's record. "It's pointing at $950. Now there's a power shortage (and) everything is in favor of gold for the time being," said Lee Cheong Gold Dealers Director Ronald Leung. Analysts noted that gold could undergo a downward correction after a U.S. Federal Reserve meeting on interest rates this week but the downside could be limited to $880 or $900. "I don't expect it to go down to $850 again if there's a correction this time," Leung
Qgo down to $850 again if there's a correction this time," Leung
said. Another industry analyst predicted the price of gold to reach $1,000 an ounce by June 2008. Platinum also reached a historic high of $1,652 an ounce. "Platinum is confronted by a big supply and demand problem. The price will be very strong in the future. Within a month, the next price target is $1,650," said Yukuji Sonoda, precious metals analyst at Daiichi Commodities. On Thursday, Lonmin, the world's third largest platinum producer, cut its sales outlook for the year after first-quarter refined platinum output slid by nearly a fifth due to safety shutdowns and persistent processing problems. (Mining Weekly, January 25, 2008)

Government Reassures Investors

¶11. (U) Minerals and Energy Minister Buyelwa Sonjica announced

that the government will do all it can to ensure that the power crisis "does not impact negatively investments," after a meeting with mining and industry leaders. South Africa is currently listed among the world's top 20 investment destinations, but recent power outages, particularly across the country's mining sector, have threatened this status. Companies lost an average of 24% of labor production as a result of this month's power cuts. Eskom estimated that supply problems will persist until 2013. "This is a temporary situation and what we are going to do is manage our way through it so that it doesn't impact on the country's growth trajectory," said Public Enterprises Minister Alec Erwin. Erwin was confident that South Africa would continue to attract investment despite the power crisis. He said it was obvious that the current situation would impact economic growth if it continued unmanaged. The government spoke with investors so that "coordinated growth in energy needs could be catered without further jeopardizing the system". Already the threat of poor power supplies had resulted in foreign companies questioning their investments, and local mining companies having to revisit expansion plans. Trade unions warned that the production stoppage in the mining industry could cost jobs, but Erwin felt this was premature. (Business Day, January 29, 2008)

CEF Funds Solar-powered Traffic Lights
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12 (U) The Central Energy Fund (CEF) announced a commitment of over $5.8 million to erect solar-powered traffic lights at major intersections in South Africa's main cities. CEF CEO Mputumi Damane noted that this effort is meant to mitigate the affects of recent power shortages, which have caused traffic jams and accidents. Cape Town City municipality successfully launched a pilot project utilizing these solar-powered traffic lights in September 2007. New installations are aimed for the cities of Ethekwini (Durban), Johannesburg, Nelspruit, Port Elizabeth, and Tshwane (Pretoria). CEF expected the capital investment required

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to complete this project to rise above $14.3 million and will be soliciting funds from private investors. Damane said investors could claim up to 150% of their investment in their next tax returns. (Business Day, January 23, 2008)

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